Blank Page

FILE COPY

Office - Supreme Court, U. S.
FILED
NOV 20 1940
CHARLES ELMORE CROPLEY
CLERK

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1940

No. 78

A. C. FROST & COMPANY,
Petitioner,

vs.

COEUR D'ALENE MINES CORPORATION.

BRIEF FOR PETITIONER.

ERNEST L. WILKINSON,
CHARLES J. KAPPLER,
JOHN W. CRAGUN,
Counsel for Petitioner.

Blank Page

INDEX.

Subject Index.

	Page
Brief for petitioner	1
Opinions below	1
Jurisdiction	1
Questions presented	2
Statutes involved	3
Specification of errors to be urged	3
Statement	3
Summary of argument	9
Argument	12
Analysis of question presented	12
The Securities Act of 1933 does not render void a contract for the purchase of securities which are not registered	15
This is not a transaction "involving any public offering"	24
Conclusion	28
Appendix	29
Statutes involved	29
Specification of errors to be urged	33

Table of Cases Cited.

Awotin v. *Atlas Exchange Nat. Bank*, 295 U. S. 209, 213	2, 14
Bank of Kentucky v. *Adams Exp. Co.*, 93 U. S. 174, 181	27
Bank of the United States v. *Owens*, 2 Pet. 527, 538, 541	14
Bement v. *National Harrow Co.*, 186 U. S. 70, 88, 94	13
Black v. *Solano Co.* (1931), 114 Cal App. 170, 177-178, 299 P. 843	25, 26
Blodgett v. *Lanyon Zinc Co.* (C. C. A. 8th, 1903), 120 Fed. 893, 896	14
Brown v. *Tarkington*, 3 Wall. 377	13
Burck v. *Taylor*, 152 U. S. 634, 648	13

Page

Cincinnati P., B. S. & P. P. Co. v. *Bay*, 200 U. S. 179, 185 ..... 13, 27
Cochran v. *Hurth*, 29 Ohio App. 305, 163 N. E. 560, 561 24
Connolly v. *Union Sewer Pipe Co.*, 184 U. S. 540, 550, 551 13
Consolidated Edison Co. v. *National Labor Relations Board*, 305 U. S. 197, 235, 236, 237 13
Coppell v. *Hall*, 7 Wall. 542, 556, 558 14
Craig v. *Missouri*, 4 Pet. 410, 436 14
Davidson v. *Lanier*, 4 Wall. 447, 454-455 14
De Wolf v. *Johnson*, 10 Wheat. 367, 392 14
Doherty v. *McAuliffe* (C. C. A. 1st, 1935), 74 F. (2d) 800, 802-3, cert. den. 294 U. S. 730 24
Dunlop v. *Mercer* (C. C. A. 8th, 1907), 156 Fed. 545 14
Embrey v. *Jemison*, 131 U. S. 336 13
Farmers', etc., Bank v. *Dearing*, 91 U. S. 29, 35-36 14
Fleckner v. *U. S. Bank*, 8 Wheat. 338, 353, 355 14
Fosdick v. *Investors Syndicate*, 266 N. Y. 130, 135 24
Fritts v. *Palmer*, 132 U. S. 282, 289 14
H. H. Miller Industries Co. v. *Roman*, 37 Ohio App. 71, 174 N. E. 141 24
Hannay v. *Eve*, 3 Cr. 242, 247-248 14
Hanover Nat. Bank v. *First Nat. Bank* (C. C. A. 8th, 1901), 109 Fed. 421, 425-6 14
Harris v. *Runnels*, 12 How. 79, 83-84 ..... 13, 27
Hobbs v. *McLean*, 117 U. S. 567, 575, 576 13
Landay v. *United States* (C. C. A. 6th, 1939), 108 F. (2d) 698, 704 20
Levering & Garrigues Co. v. *Morrin*, 289 U. S. 103, 105 2
Logan County Bank v. *Townsend*, 139 U. S. 67, 75-76 14
Louisville & N. R. Co. v. *Mottley*, 219 U. S. 468, 477-479 14
McBroom v. *Scottish Mtg. & Land Inv. Co.*, 153 U. S. 318, 323 13
McNair v. *Knott*, 302 U. S. 369, 371 13
Milheim v. *Moffat Tunnel Dist.*, 262 U. S. 710, 716 2
Mower v. *Fletcher*, 114 U. S. 127 2

Page

Nash v. *Lynde* [1929] A. C. 158, 169 25
National Bank v. *Matthews*, 98 U. S. 621, 627 ..... 13, 14
National Bank v. *Whitney*, 103 U. S. 99, 102 14
Oates v. *National Bank*, 100 U. S. 239, 250 14
People v. *Ruthven* (1936) 160 Misc. 112, 288 N. Y. Supp. 631, 636-637 26
Robertson v. *Business Boosters Country Club*, 212 Ala. 621, 622-3, 103 So. 576, 577 24
Sajor v. *Ampolin*, 275 N. Y. 125, 131, 9 N. E. (2d) 803, 805-6 24
Securities & Exchg. Comm. v. *Federal Compress & Whs. Co.*, 88 F. (2d) 1018 26
Securities and Exchange Commission v. *Sunbeam Gold Mining Co.*, C. C. A. 9, 1938, 95 F. (2d) 699 ..... 12, 24, 27
Sherwell v. *Incandescent Mantles Syndicate* (1907), 23 T. L. R. 482, 51 Sol. Jo. 446 26
Smith v. *McCullough*, 270 U. S. 456, 463-465 14
Stansbury v. *United States*, 8 Wall. 33 13
Steele v. *Drummond*, 275 U. S. 199 16
Texas and Pac. Ry. Co. v. *Pottorff*, 291 U. S. 245, 255 14
Thompson v. *St. Nicholas National Bank*, 146 U. S. 240, 251 ..... 13, 14
Twin City Pipe Line Co. v. *Harding Glass Co.*, 283 U. S. 353, 357 12
Union Gold-Mining Co. v. *National Bank*, 96 U. S. 640, 642 13
Union Nat. Bank v. *Matthews*, 98 U. S. 621, 627 13
Wood v. *Lady Duff-Gordon*, 222 N. Y. 88, 91 16

TABLE OF STATUTES AND OTHER AUTHORITIES.

Act of June 25, 1938, c. 677, 52 Stat. 1070, 1076, § 3 ..... 11, 22
English Companies Act of 1929, 19 and 20 Geo. 5, c. 23 15
Judicial Code, § 237(b) 2
Trust Indenture Act of 1939, c. 411, 53 Stat. 1149, 1177, § 327 11
Uniform Sale of Securities Act, 9 Uniform Laws Ann., 387, § 16 23

Page

Securities Act of 1933, c. 38, Title I, 48 Stat. 74, 77, 15 U. S. C. § 77a et seq.:
- Generally 3, 9, 10, 15, 18, 21
- § 4 ..... 2, 11, 24, 28
- § 5 ..... 2, 12, 15
- § 6 20
- § 7 20
- § 12 ..... 10, 14, 15, 17, 19
- § 14 ..... 10, 16, 18
- § 20 15

Securities Exchange Act of 1934, c. 404, 48 Stat. 881, § 29 ..... 11, 21, 23

Rules of the Securities and Exchange Commission, Rule 152 ..... 12, 26

Congressional Record:
- Message of the President, vol. 77, p. 2923 18
- Statement of Mr. Rayburn, vol. 77, pp. 2918, 2919 ..... 18, 19
- Statement of Sen. Fletcher, vol. 77, p. 2983 18

Congressional Hearings on Securities Act of 1933:
- House 19
- Senate 19

Douglas and Bates, Some Effects of the Securities Act upon Investment Banking (1933), 1 U. Chic. L. Rev. 283, 299 25

Note, 87 A. L. R. 98 on State Blue Sky Laws 23, 24

Opinion, General Counsel S. E. C., Release No. 285 25

Susman, Exempted Transactions under the Securities Act of 1933, 24 Wash. U. L. Q. 383, 386 25

Williston on Contracts (rev. ed.) 16

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1940

No. 78

A. C. FROST & COMPANY,

Petitioner;

vs.

COEUR D'ALENE MINES CORPORATION.

BRIEF FOR PETITIONER.

Opinions Below.

The trial court rendered no written opinion, but adopted findings of fact and conclusions of law which appear at R. 205-218.

The opinion of the Supreme Court of the State of Idaho (R. 226), as modified following a petition for rehearing (R. 235), appears in 98 P. (2d) 965, and is not yet officially reported.

Jurisdiction.

The judgment of the Supreme Court of the State of Idaho was entered December 15, 1939 (R. 226). A petition for rehearing was entertained; and the opinion originally an-

nounced was modified February 15, 1940 (R. 235), at which time the petition for rehearing was denied. The petition for certiorari was filed in this Court May 15, 1940. The writ of certiorari was granted October 14, 1940.

The jurisdiction of this Court rests on Section 237 (b) of the Judicial Code as amended. The statute of the United States which is involved is the Securities Act of 1933 (Act of May 27, 1933, c. 38, Title I, 48 Stat. 74, 77 §§4 and 5, Title 15 U. S. C., §§ 77 d, e). The judgment of the Supreme Court of the State of Idaho directs entry of a final judgment against petitioner. It is, therefore, final for purposes of this Court's jurisdiction. *Mower* v. *Fletcher*, 114 U. S. 127. The Supreme Court of the State of Idaho founded its decision on its interpretation of the Securities Act of 1933, holding that a contract for the sale of stock not registered under the Securities Act of 1933 is void as violative of the spirit or intent of the Act, and that the transaction is not exempted by that Act. The question involved has not heretofore been passed upon by this Court. No provision of the Securities Act of 1933 purports to declare such a contract void; and counsel have found no opinion except that here sought to be reviewed which accords with the decision below.

The federal question is, therefore, substantial. *Levering & Garrigues Co.* v. *Morrin*, 289 U. S. 103, 105; *Milheim* v. *Moffat Tunnel Dist.*, 262 U. S. 710, 716. Whether a contract is illegal under a Federal statute is a federal question which this Court has jurisdiction to review. *Awotin* v. *Atlas Exchange Nat. Bank*, 295 U. S. 209, 213.

Questions Presented.

1. Whether an option to purchase directly from the issuing company certain shares of its stock from time to time is void as to the purchaser where the issuer has failed to register the stock with the Securities and Exchange Commission under the provisions of the Securities Act of 1933.

2. Whether a transaction under which one who takes an

option to purchase substantially all the shares of stock of a corporation remaining in its treasury and who subsequently waives the right to take some of the shares to permit their sale to others, is a transaction "involving any public offering" (Sec. 4(1), clause 2, Securities Act of 1933).

Statutes Involved.

The statutes involved are set forth in the appendix, *infra*, pp. 29-33.

Specification of Errors to be Urged.

The specifications of errors to be urged are set forth in the appendix, *infra*, p. 33.

Statement.

This was an action brought by petitioner against respondent in an Idaho state court to recover for breach of a contract by which respondent was to sell certain stock to petitioner. Respondent defended on the ground, among others, that the original agreement of the parties was entered into in violation of the Securities Act of 1933, in that the shares of stock attempted to be sold "had never been registered for sale under said National Securities Act, or Acts amendatory thereof or supplemental thereto, with the Securities & Exchange Commission", and that "said contract was void, ab initio" (R. 186). Other grounds of defense were bottomed on non-federal questions.

The findings of the trial court (R. 205-218) may be summarized as follows:

Respondent entered into a contract September 10, 1934, with one Boland, wherein respondent undertook to sell, of its 3,000,000 shares authorized capital stock, the 1,300,000 shares of stock which remained in its treasury at 10 cents a share, payments to be made from month to month as specified, and shares to be issued as paid for, without liability on the part of the purchaser for failing to purchase the entire lot of 1,300,000. (Throughout, this has been referred

to as the option agreement.) Finding 3, R. 209. Respondent represented that it was authorized to sell and deliver the 1,300,000 shares of treasury stock upon such terms as it might deem proper. *Id.* On the same day, Boland assigned the contract to petitioner; and petitioner acted and was accepted as the owner of the option granted by the contract. Finding 4, R. 210. In the negotiation of the contract Boland had acted as agent for the plaintiff. *Id.* The option agreement was thereafter modified as to dates and amounts of monthly payments on April 26, 1935. Finding 5, R. 211. On May 15, 1935, petitioner and respondent agreed that proceeds from the sale of treasury stock[1] after the sale of the next twenty thousand shares should be retained in respondent's treasury for the purpose of speedy development of the mining property of respondent and purchase of equipment, purchase of additional mining property (the "Mineral Point Mine") and reimbursement of certain advances to respondent and the construction of a mill within six months. Finding 6, R. 212. It was further agreed that all credits over and above 10 cents per share would be placed to petitioner's credit with interest at 6% per annum, to be reimbursed to petitioner from the first earnings of the property. *Id.* Amounts realized from the sale of treasury stock by Mr. Nuzum (respondent's President) were to remain in the treasury of respondent, crediting petitioner for the proceeds over 10 cents per share. *Id.* Payments in accordance with the option agreement as modified totalling $16,500 (for which petitioner received 165,000 shares of stock) were made from month to month from September 10, 1934, to March 22, 1935. Findings 7 and 8, R. 213. In

---

[1] These sales of stock to others than petitioner apparently were not contemplated in the original agreement, but came subsequently when petitioner had encountered some trouble in meeting the terms of the agreement as originally undertaken. See the statement of facts in addition to the specific findings of the trial court, *infra*, pp. 6-8.

addition, petitioner caused to be paid to respondent the option price of 10 cents per share for 279,850 shares of the treasury stock sold to other parties than the petitioner.[2] Included in these sales were sales of 80,000 shares to E. J. Gibson & Company on May 8, 1935, and 20,000 shares to J. E. Jones Brokerage Company in June, 1935. These payments received by respondent were sufficient to pay the amounts due under the option agreement through the payment due in July, 1935, leaving $500 to apply on the August, 1935, payment. The proceeds of sales of stock made to others than petitioner were sufficient to meet payments up to and including that due on October 10, 1935. Finding 8, R. 214. By reason of the petitioner's inability to finance purchase of the stock and to have the stock registered with the Securities & Exchange Commission, petitioner abandoned the option to purchase the remainder of stock covered by the agreement in the summer of 1935. Finding 9, R. 214; Finding 11, R. 215. During the month of June, 1935, respondent refused to deliver more stock to petitioner on the ground that the stock had not been registered with the Securities and Exchange Commission, and refused to perform the agreement further until authority was obtained for the sale of the stock under the Securities Act of 1933. Finding 10, R. 215. The shares of stock of respondent covered by the option agreement were never registered for sale under the Securities Act of 1933. *Id.* On March 13, 1936, respondent notified petitioner of the termination of the option agreement on the ground of failure by petitioner to perform. Finding 11, R. 215. Petitioner had failed to perform the contract even though respondent had not refused to perform nor repudiated its obligations by the notice in June, 1935. *Id.* Mr. Nuzum (respondent's President) sold 90,000 shares of treasury

[2] A complete statement covering the 279,850 shares, as prepared by respondent, appears as Exhibit 74. Testimony covering this Exhibit appears (R. 94-95).

stock at 19 cents per share and 89,850 shares of treasury stock at various prices, in accounting for which respondent owes petitioner $16,306.[3] Finding 16, R. 216. The court concluded that the option agreement of September 10, 1934, was entered into in violation of the Securities Act of 1933 and is not enforceable as to unexecuted portions thereof; that petitioner had abandoned the option agreement in the summer of 1935 and forfeited its rights under the option agreement with respect to further performance; and that petitioner was not entitled to judgment save for the $16,306 mentioned above. R. 218.

From the judgment predicated on the foregoing findings and conclusions, both parties appealed to the Supreme Court of Idaho.

A further statement of matters established by the record will be of assistance in understanding some features of the Federal question involved:

At the time petitioner took the option to purchase the shares in the treasury of respondent, respondent owned an option to purchase certain mining properties (referred to throughout the record as the Mineral Point Group). R. 175. The purpose of the sale of respondent's shares contemplated by petitioner's option seems to have been to develop and equip the Mineral Point Mine. R. 177. When petitioner ran into difficulties financing the purchase of the shares, he at first secured an extension of the terms of the option, not wishing to market any stock. Although the stock was selling on the market at twice the option price, petitioner did not want to market any of the stock and Mr. Nuzum had agreed that it should not be marketed until it had value

[3] How this is arrived at is not stated in the findings of the trial court. The amount found due represents the difference between 10 cents per share which petitioner would have had to pay under the option agreement and the amount received by respondent upon the sales through its president to others than petitioner. These shares are part of the lot of 279,350 shares mentioned in Finding 8 (R. 214). See Exhibit 74.

sufficient to pay for the property. R. 64. Petitioner agreed to release stock from its option in order that it might be used as part of the purchase price for the Mineral Point Claims. Ex. 37. The modification of the petitioner's option May 11, 1935, contemplated use of the money received from sale of shares for the purpose of paying for the Mineral Point Mine. R. 212. Petitioner's president pointed out the necessity of completing the purchase of the Mineral Point property. Ex. 33; *cf.* Exs. 35, 37. Sale of the stock was apparently considered by the parties as a means of securing the money necessary for this purchase. Exs. 37; 38. To accomplish that, there was recognized the necessity for registering the stock with the Securities and Exchange Commission and listing on a stock exchange; and accordingly, petitioner's president wrote many letters to respondent, emphasizing the importance of registering the stock. R. 41 *et seq.*; see Exs. 33, 34, 35, 36, 37, 38, 39, 40, 68, 41, 64, 65. Although obviously only respondent could actually execute the registration statement, petitioner secured the forms of application for listing and registration of the stock. Ex. 37. He even prepared the forms so far as he could, making copies of papers to accompany the blanks.[4] R. 61; Ex. 39. Ultimately petitioner was advised by respondent that the stock could not be listed with the Securities Exchange for the reason that "we would have to show title to the property or the certificate will not be granted".[5] Ex. 63.

There is no evidence to show that petitioner sold the shares which it acquired under the option, or that it bought them for resale. There is evidence to show that petitioner

---

[4] Respondent's president, Mr. Nuzum, was an attorney at law (R. 142). Apparently petitioner's president, Mr. Frost, entertained the notion during part of this time that listing on a stock exchange did away with the necessity for registering the stock under the Securities Act (Ex. 36).

[5] It is to be understood that Mr. Nuzum was talking of the Mineral Point property, as to which respondent had only an option.

either sold itself or acquiesced in the sale by respondent of certain shares to which it would have been entitled under the option, and shared in the proceeds of such sales, these sales being to E. J. Gibson & Co. (80,000 shares) and J. E. Jones Brokerage Co. (20,000 shares). See *infra*, p. 26, note 19. It also appears that petitioner "acquiesced" in the sale by respondent's president Nuzum of some 90,000 shares, although petitioner did not, apparently, have anything to do with the making of those sales.[6] R. 37

The record is deficient in explaining the purposes the parties may have had in mind in entering into the option agreement. It is not shown that this was an underwriting enterprise, whereby petitioner was to take and retail an entire issue of stock in exchange for immediate operating capital given to respondent, or agreed to take so many shares as respondent could not sell to the public. On the other hand, the record does not satisfactorily show that petitioner bought the stock purely as an investment. It is shown that after the option agreement had been in force some months, sales of some of the shares were contemplated in order to finance development of the property, and that petitioner was anxious to have the stock registered and listed on a stock exchange so that sales could be made of the remaining treasury stock not taken up by petitioner.

Upon the respective appeals of the parties, a majority of the Supreme Court of Idaho thought that the dealings between petitioner and respondent were in contravention of Section 5(a) of the Securities Act of 1933 providing against use of interstate means of communication, transportation or

---

[6] As a matter of fact, petitioner did not even know the extent of those sales until the trial below. Thus, petitioner had alleged the sale by respondent of 90,000 shares (R. 174). But at the trial it developed (R. 95, 118-123, Ex. 74) that respondent's president had sold the larger number, and had credited petitioner with the excess received over the purchase price. Accordingly, petitioner was allowed (R. 204) to amend its complaint to accord with the proofs.

the mails in connection with sales or deliveries of securities. It thought that there was no exemption from this provision by reason of Section 4, which exempts transactions by an issuer not involving any public offering. As showing that the contract was void, it relied upon the provisions of an entirely different act (Securities Exchange Act of 1934) which declares void every contract the performance of which involves violation of the provisions of that act.[7] The majority of the Court thought that since the option agreement was void because prohibited by law or public policy, the court would leave the parties in the identical situation in which it finds them and the contract cannot be treated as valid by invoking estoppel. The court, therefore, reversed the judgment which had been granted petitioner for the profits realized by respondent on sales of stock to which petitioner was entitled before the option was claimed to have lapsed; and it affirmed as to the cause of action seeking damages for the claimed breach of the contract.

Summary of Argument.

1. The court below held the contract in suit void on grounds of public policy. Public policy is primarily for the lawmakers to determine. There is no express provision of the Securities Act of 1933 which declares contracts for the sale of unregistered securities void. Accordingly, the court must consider the entire statute generally and its aims specifically to determine whether the legislature intended to make the contract void. In such cases this Court has looked to the purposes and policy of the legislative to determine the policy of the law, and has held contracts enforcible or illegal in accordance with the policy so found. Since Congress has dealt with the effect of violations of

[7] This ground of the decision was eliminated following the petition for rehearing (R. 235).

the act upon contracts to sell unregistered shares, the court may not add a penalty of its own making (by declaring the entire contract void) to the penalties decreed by Congress.

This case involves no question of the right of a purchaser to rescind, or of the right of the Securities and Exchange Commission on behalf of the public to enjoin violations of the act or compel registration of securities. Nor does it involve any question of criminal violation of the act.

2. Section 14 of the act declares void only those provisions or conditions which bind a purchaser of securities to waive compliance with any provision of the act. The contract in suit contains no such provision but affirmatively represents that respondent is authorized to sell and deliver the securities. Accordingly, the obligation to register was assumed by respondent in the contract it now attacks. Section 12 of the act recognizes that securities may be sold without a registration statement being in effect and determines the consequences which shall flow from such sales. No further consequence, as declaring invalid an agreement for sale of unregistered stock, was contemplated by Congress.

The policy of the Securities Act is to enforce truth in the sale of securities, not to prohibit dealings in securities. The legislative history of the act recognizes this, and also shows that registration was not essential to dealings in securities. The policy of Congress was to make those who failed to register substantially insurers of the value of the securities as to members of the public deprived of information. But no intent on the part of Congress to prohibit such dealings can be found.

By the act the duty to register was on respondent; only respondent could accomplish the registration. Accordingly, the policy of Congress is not served by permitting respondent to escape its obligations by pleading its violation of the

statute. The decision below would encourage violation of the act, and in any event does not accord with the purposes of Congress.

The fact that Congress did not intend to declare dealings in securities unlawful if the securities were not registered is shown by acts *in pari materia* with the Securities Act of 1933. Securities Exchange Act of 1934, § 29; Trust Indenture Act of 1939, § 327; Act regulating over-the-counter brokers and dealers, June 25, 1938, c. 677, 52 Stat. 1070, 1076, § 3.

Cases under state blue sky laws show a varying policy on the part of the states and varying statutory provisions and legislative policies as to whether contracts to deal in unlicensed securities shall be void, voidable, or valid and enforceable.

3. The court below held the stock ought to have been registered and was not exempt from registration under Section 4(1) of the Securities Act. It thought that petitioner was "selling the treasury stock to all and sundry", so that the transaction involved a "public offering".

The only offer involved was the offer of respondent in the option agreement to sell all of its treasury stock to but one person, petitioner. The offer was not to the public. No issue is properly in the case as to whether sales of stock to others than petitioner were made to the public or were made pursuant to a public offering; and those sales do not concern the question whether the securities ought to have been registered before they were sold to petitioner.

Whether an offering is a "public offering" is largely a question of fact; and the offering is to be distinguished from the sale. Here, however, there was an offering to but one person who possessed a special knowledge of respondent and took particular interest in respondent's affairs. The transaction with petitioner is expressly exempt as a public

offering under Rule 152 of the Securities and Exchange Commission.

Furthermore, there is nothing in the record to support the statement of the court below that petitioner was "selling the treasury stock to all and sundry".

Securities and Exchange Commission v. *Sunbeam Gold Mining Co.*, C. C. A. 9, 1938, 95 F. (2d) 699, does not support the decision in this case; for here there is an offering of all the shares to petitioner, which put it beyond the power of respondent to offer any shares to the public while the agreement remained unchanged. The subsequent amendment of the agreement to permit sales of the shares to other than petitioner does not affect the result, since it will not be presumed that those sales were to be made in violation of law.

ARGUMENT.

I.

Analysis of Question Presented.

The Supreme Court of Idaho held that the contract involved was within the purview of the Securities Act of 1933; that it violates that act, in that the stock was not registered as required by the act; and that it is, therefore, void on grounds of public policy. If the contract comes within the requirements of §5 of the Securities Act for registration of stock, the question is whether respondent, who issued the stock, shall escape its contract by reason of the fact that it failed to register the stock. Or stating it another way, the question is: What public policy requires that this contract be held void?

Public policy is primarily for the lawmakers to determine. *Twin City Pipe Line Co.* v. *Harding Glass Co.*, 283 U. S. 353, 357. Primarily, therefore, we are to refer to the Securities Act of 1933 to determine whether Congress intended to make an option agreement such as that here involved.

void. There is no provision in the Securities Act of 1933 which declares contracts for the sale and purchase of unregistered securities to be void (nor even a provision which forbids the formation of such contracts).

In such circumstances the court must consider the entire statute generally and its aims specifically to determine whether the legislature intended to make the contract void. *Harris* v. *Runnels,* 12 How. 79, 84; *Union Nat. Bank* v. *Matthews,* 98 U. S. 621, 627; *McBroom* v. *Scottish Mtg. & Land Inv. Co.,* 153 U. S. 318, 323; *Union Gold Mining Co.* v. *National Bank,* 96 U. S. 640, 641. *Cf. Thompson* v. *St. Nicholas National Bank,* 146 U. S. 240, 251; *Burck* v. *Taylor,* 152 U. S. 634, 648. Many cases typify the application of this rule. Time and again when this Court has had under consideration the question whether a contract was invalid because it contravened a statute (though the statute did not expressly make contracts invalid),[8] the Court has looked to the purposes and policy of the legislative in order to determine whether invalidity of the contract accords with that policy. Where the policy of Congress has not required that a contract be struck down, the Court has enforced it. *Harris* v. *Runnels,* 12 How. 79, 83-84, *et passim*; *Union National Bank* v. *Matthews,* 98 U. S. 621, 627; *National Bank* v. *Whitney,* 103 U. S. 99, 102; *Union Gold-Mining Co.* v. *National Bank,* 96 U. S. 640, 642; *Connolly* v. *Union Sewer Pipe Co.,* 184 U. S. 540, 550, 551; *Bement* v. *National Harrow Co.,* 186 U. S. 70, 88, 94; *Cincinnati P., B. S. & P. P. Co.* v. *Bay,* 200 U. S. 179, 185; *Hobbs* v. *McLean,* 117 U. S. 567, 575, 576. *Cf. Consolidated Edison Co.* v. *National Labor Relations Board,* 305 U. S. 197, 235, 236, 237; *McNair* v. *Knott,* 302 U. S. 369, 371.

---

[8] We may lay out of consideration the many cases which hold that a contract expressly made void by statute can be enforced by neither party. See, *e. g., Embrey* v. *Jemison,* 131 U. S. 336, 344-346; *Brown* v. *Tarkington,* 3 Wall. 377, 381; *Stansbury* v. *United States,* 8 Wall. 33, 36-37.

Where, however, it has been found that it was within the purpose or policy of Congress to hold the contract illegal, it has not been enforced at the instance of a wrongdoer. *Davidson* v. *Lanier*, 4 Wall, 447, 454-455; *Hannay* v. *Eve*, 3 Cr. 242, 247-248; *Awotin* v. *Atlas Exchange Nat. Bank*, 295 U. S. 209, 212; *Louisville & N. R. Co.* v. *Mottley*, 219 U. S. 468, 477-479; *Smith* v. *McCullough*, 270 U. S. 456, 463-465; *Texas and Pac. Ry. Co.* v. *Pottorff*, 291 U. S. 245, 255; *Bank of the United States* v. *Owens*, 2 Pet. 527, 538-541. *Cf. Craig* v. *Missouri*, 4 Pet. 410, 436; *Coppell* v. *Hall*, 7 Wall. 542, 556, 558.

In the present case the statute does deal with the effect of violations of the act upon contracts to sell unregistered shares (see point II, *infra*). In such a situation the court may not add a penalty of its own making (that is, to declare the entire contract void) to the penalties expressly decreed by Congress. *Fritts* v. *Palmer*, 132 U. S. 282, 289; *National Bank* v. *Matthews*, 98 U. S. 621, 627; *De Wolf* v. *Johnson*, 10 Wheat. 367, 392; *National Bank* v. *Whitney*, 103 U. S. 99, 102; *McBroom* v. *Scottish Mtg. & Land Inv. Co.*, 153 U. S. 318, 323-4; *Oates* v. *National Bank*, 100 U. S. 239, 250; *Fleckner* v. *U. S. Bank*, 8 Wheat. 338, 353, 355; *Farmers', etc., Bank* v. *Dearing*, 91 U. S. 29, 35-36; *Dunlop* v. *Mercer* (C. C. A. 8th, 1907), 156 Fed. 545; Sanborn, J., in *Hanover Nat. Bank* v. *First Nat. Bank* (C. C. A. 8th, 1901), 109 Fed. 421, 425-6; *Blodgett* v. *Lanyon Zinc Co.* (C. C. A. 8th, 1903), 120 Fed. 893, 896. *Cf. Thompson* v. *St. Nicholas Nat. Bank*, 146 U. S. 240, 251; *Logan County Bank* v. *Townsend*, 139 U. S. 67, 75-76.

It should be noted that this case does not present any question of the rights of a purchaser of unregistered securities to rescind his contract or recover damages under § 12. Rescission is a remedy given solely to a purchaser of stock, and obviously could not be exercised by the vendor, respondent in this case. This case involves no question of the right

of the Securities and Exchange Commission on behalf of the public to enjoin a threatened violation of the Securities Act of 1933, or affirmatively to compel registration of securities under § 20(b) and (c) of the Securities Act. This case involves no question of criminal violation of the Securities Act of 1933; it has never been suggested that any device, scheme or artifice to defraud in the sales of respondent's stock have been undertaken by petitioner.

Having in mind then that the question is solely whether the transaction here involved violates the Securities Act of 1933 and whether, if it does, the contract for the purchase of these shares by petitioner is void, we turn to the Securities Act of 1933 as the best expositor of the public policy involved.

II.

The Securities Act of 1933 Does Not Render Void a Contract for the Purchase of Securities Which Are Not Registered.

Assuming that the shares of the respondent's stock here involved ought to have been registered with the Securities and Exchange Commission (see point III, *infra*, p. 24), we consider first the provisions of the act which deal with contracts violating its terms.

Section 14 deals expressly with invalidity of contracts involving violations of the act, stating:[9]

---

[9] This provision appears to be drawn from the equivalent English statute, the Companies Act of 1929, 19 and 20 Geo. 5, c. 23, § 35(2), which provides:

> "(2) A condition requiring or binding an applicant for shares in or debentures of a company to waive compliance with any requirement of this section, or purporting to affect him with notice of any contract, document, or matter not specifically referred to in the prospectus, shall be void."

And with § 5 of the Securities Act of 1933, compare § 35(3) of the English statute; and with § 12 of the Securities Act, *infra*, compare § 37(1) of the English statute.

"Any condition, stipulation, or provision binding any person acquiring any security to waive compliance with any provision of this title or of the rules and regulations of the Commission shall be void."

This option agreement contains no stipulation that petitioner will waive compliance with any provision of the act or the rules and regulations thereunder. Quite the contrary. The option agreement contains the express representation on the part of respondent that of its three million shares of capital stock there remain in the treasury 1,300,000 shares, "which the said party of the first part [respondent] *is authorized to sell and deliver* upon such terms as it may deem proper." (R. 175.) If in fact, registration of the stock were necessary—as respondent has contended throughout in this action—the contract was at least "instinct with an obligation" upon respondent to register the shares.[10] *Wood* v. *Lady Duff-Gordon*, 222 N. Y. 88, 91. But if respondent had not contracted to register the stock, still § 14, under the ordinary rule *expressio unius*, would indicate the contracts which do not contain a provision waiving compliance with the Securities Act are entirely valid and enforcible.

---

[10] The case is, therefore, at least once removed even from that class of cases as to which Professor Williston states (Williston on Contracts, Rev. ed., § 1767, vol. 6, p. 5018):

> "In general, unless a bargain necessarily contemplates an illegal act, it is not unenforceable, and if it is later performed in a way that involves some slight violation of law, not seriously injurious to the public order, the person performing may recover on his bargain."

Or, as the same author states (*ibid.*, note 3):

> "The fact that a party bargains to do an act which will be illegal unless governmental permission is obtained does not make such bargain illegal, and if he does not obtain such permission he is responsible in damages for failure to perform."

—citing, *inter alia*, *Steele* v. *Drummond*, 275 U. S. 199. On this doctrine, respondent is liable rather than immune because of its failure to register.

Another provision of the act, § 12, provides:

"Any person who——

"(1) sells a security in violation of section 5, or

"(2) sells a security (whether or not exempted by the provisions of section 3, other than paragraph (2) of subsection (a) thereof, by the use of any means or instruments of transportation or communication in interstate commerce or of the mails, by means of a prospectus or oral communication, which includes an untrue statement of a materi[illegible]fact or omits to state a material fact necessary in orde[illegible]ake the statements, in the light of the circumstances u[illegible]der which they were made, not misleading (the purchaser not knowing of such untruth or omission), and who shall not sustain the burden of proof that he did not know, and in the exercise of reasonable care could not have known, of such untruth or omission,

"shall be liable to the person purchasing such security from him, who may sue either at law or in equity in any court of competent jurisdiction, to recover the consideration paid for such security with interest thereon, less the amount of any income received thereon, upon the tender of such security, or for damages if he no longer owns the security."

The right of rescission provided in § 12 is not available to the vendor (respondent); and § 12 expressly recognizes that unregistered stock may be *sold*, since it provides for liability of one "who *sells* a security in violation of section 5".

It is, therefore, apparent from the face of the statute itself that Congress had fully in mind the question as to what incidents should flow from failure to register and from dealings in unregistered stock. In certain circumstances, a purchaser may rescind. This right of recission in the events named by Congress would be wholly illusory if Congress had intended that the contract should be void at the

instance of the issuer. Congress has made express provision in § 14 as to the extent to which a contract shall be invalid—and has failed to strike down any other provisions than those which stipulate against compliance with the act. As we have shown above (p. 14), the established rule is that where Congress has stated what limited effect upon a contract non-compliance with the law shall have, the courts cannot add a judicial penalty to that adopted by the legislature by denouncing the entire agreement.

No other policy than that which Congress has thus plainly expressed can be found from an examination of the act as a whole. That act is one to enforce truth in the public sale of securities. Untruths, frauds and deceits are punished in the penal sections of the act; and remedies for losses, incurred from no affirmative fraud, but rather from failure to comply with the provisions requiring full disclosure of the truth, are established. The object is not to prohibit dealings in securities, but to afford a remedy to those damaged from failure to make full disclosure of the facts bearing on the value of securities.

The legislative history of the Securities Act of 1933 bears out what is obvious from the face of the act itself—that the policy is that issues of new securities should be accompanied by full publicity and information,[11] and, so far as available information is concerned, to place the buyer on the same plane with the management of the corporation.[12]

There are miscellaneous statements in the course of the consideration of the bill which became the Securities Act

---

[11] See message of the President recommending the adoption of securities legislation, 77 Cong. Rec. 2923.

[12] Statement of Mr. Rayburn, Chairman of the Committee on Interstate and Foreign Commerce, when the bill was being considered on the floor of the House. 77 Cong. Rec. 2918.

Statement of Senator Fletcher, Chairman of the Senate Committee on Banking and Currency, to the Senate, 77 Cong. Rec. 2983.

which indicate that the bill did not in all events require the registration of securities sold to the public.[13]

We know that although there was placed before the committees a study showing that under state blue sky laws contracts to deal in unlicensed securities are very frequently held void or voidable,[14] no provision was incorporated to provide for the same result in the federal law. The scheme adopted seems rather to make those who fail to register the stock substantially insurers of the securities with respect to members of the general public who were deprived of information (see § 12, *supra*). If promoters of an issue are willing to assume this insurer's liability incurred through dealings with the public in non-registered stock, it is most difficult to find any intent on the part of Congress to prohibit such dealings.

---

[13] See statement of Chairman Rayburn before the House. "This bill says to the man who issues a security, 'you may register that security; you are not compelled to register that security, but if you do not register it and you sent it through interstate commerce we will penalize you.'" 77 Cong. Rec. 2919.

The same theory was advanced by those who were instrumental in the drafting of the bill. Mr. Huston Thompson, a former member of the Federal Trade Commission who was prominent in the original or early drafting of the bill, testified before the House Committee as follows:

> "I guess there must be a misunderstanding here. The registry is not a thing which they are compelled to do. It simply provides that, in the event they do not, they suffer the penalty. It is not a thing that is absolutely required. It is not a thing that is absolutely required of them, compulsory. It is a voluntary matter. Of course, if they do not, then they subject themselves to this penalty • • • Of course, they can go ahead and sell, but if they do not register, then they subject themselves to the penalties, but we do not say that they have got to come in and register. Of course if they do not register, then they will be subjecting themselves to the penalties of the bill." Hearings, House Committee on Interstate and Foreign Commerce, on H. R. 5480, 73d Cong., 1st Sess., pp. 61-62.

[14] Hearings, Comm. Banking and Currency of the Senate, on S. 875, 73d Cong., 1st Sess., pp. 321-322; hearings before House Committee on Interstate and Foreign Commerce, *supra*, note 13, p. 97.

Furthermore, a review of the act as a whole indicates that the duty to register was upon respondent.[15] Section 6 of the act primarily relates to registration of securities. That section provides that any security may be registered by filing a registration statement which "shall be signed by each issuer, its principal executive officer or officers, its principal financial officer, its comptroller or principal acting officer, and the majority of its board of directors or persons performing similar functions". Only the issuer (except in the case of one who controls an issuer, which is not this case) has access to the information and has ability to secure the information required in the statement by section 7. Only the issuer can execute the statement required by section 6.

In this situation where the shares, as respondent says, ought to have been registered, and where respondent itself under the statute ought to have done the registering, and where petitioner did everything it reasonably could to induce the registration, it cannot accord with the statutory policy to permit respondent to escape its obligations by pleading its own wrong. The rule adopted by the court below encourages an issuer to withhold registration in any case where the issuer foresees a profit from abandoning an earlier agreement to sell stock. If any policy is manifested by the statute to penalize dealings in unregistered securities, it is to penalize respondent in some manner provided for

---

[15] We need not consider cases in which a person in actual control of an issuer such as respondent would be called upon himself to register the issuer's shares in default of the issuer itself registering them, as perhaps is contemplated by Section 2(11) of the act. We know in this case that petitioner was not in control of respondent, for not only did petitioner do everything it could to induce respondent to register the shares, only to have respondent procrastinate and refuse to register them, but obviously petitioner's contract would not have been repudiated by respondent if petitioner had control. Nor did respondent at any time in the courts below assert as a defense to this action that petitioner itself was under a duty to register the shares. *Cf. Landay* v. *United States* (C. C. A. 6th, 1939), 108 F. (2d) 698, 704.

by the act; and that policy does not sanction a reward to respondent for its noncompliance through permitting it to escape the burdens of its bargain.

This view is made even more compelling when we consider a statute *in pari materia*, the Securities Exchange Act of 1934, c. 462, 49 Stat. 1375. That act (§ 29) [16] expressly provides that:

> "(a) Any condition, stipulation, or provision binding any person to waive compliance with any provision of this title or of any rule or regulation thereunder, or of any rule of an exchange required thereby shall be void.
>
> "(b) Every contract made in violation of any provision of this title or of any rule or regulation thereunder, and every contract (including any contract for listing a security on an exchange) heretofore or hereafter made the performance of which involves the violation of, or the continuance of any relationship or practice in violation of, any provision of this title or any rule or regulation thereunder, shall be void (1) as regards the rights of any person who, in violation of any such provision, rule, or regulation, shall have made or engaged in the performance of any such contract, and (2) as regards the rights of any person who, not being a party to such contract, shall have acquired any right thereunder with actual knowledge of the facts by reason of which the making or performance of such contract was in violation of any such provision, rule or regulation."

The Securities Exchange Act of 1934 contained amendments to the Securities Act of 1933 (here directly involved), c.

---

[16] Section 29(b) of the Securities Exchange Act was relied upon by the court below (R. 229-230) in the mistaken notion that it was applicable to the case at bar. Although the Securities Exchange Act appended to its provisions certain amendments to the Securities Act of 1933, the provision of § 29 relates only to the different subject matter of the Securities Exchange Act itself. This ground of the decision was, accordingly, struck out upon the rehearing, although the conclusion that the court drew therefrom was allowed to stand (R. 235).

404, 48 Stat. 881, 905, Title 2. Congress thus plainly had before it the question of whether contracts should be void. It provided they should be void in the circumstances above named as to transactions within the Securities Exchange Act of 1934. Although dealing with the Securities Act of 1933 in the same Act, Congress made no similar provision with respect to the Securities Act of 1933.

Congress gave further consideration to the question of invalidity of contracts in connection with the act regulating over-the-counter brokers and dealers (by amendment to the Securities Exchange Act of 1934, *supra*). Act of June 25, 1938, c. 677, 52 Stat. 1070, 1076, § 3. The provision adopted by Congress in that act adds the following proviso to § 29 of the Securities Exchange Act of 1934:

> "*Provided,* (A) That no contract shall be void by reason of this subsection because of any violation of any rule or regulation prescribed pursuant to paragraph (2) or (3) of subsection (c) of section 15 of this title, and (B) that no contract shall be deemed to be void by reason of this subsection in any action maintained in reliance upon this subsection, by any person to or for whom any broker or dealer sells, or from or for whom any broker or dealer purchases, a security in violation of any rule or regulation prescribed pursuant to paragraph (1) of subsection (c) of section 15 of this title, unless such action is brought within one year after the discovery that such sale or purchase involves such violation and within three years after such violation."

Another act *in pari materia* with the Securities Act of 1933 is the Trust Indenture Act of 1939. Act of August 3, 1939, c. 411, 53 Stat. 1149, 1177, Section 327. That act provides simply, as does the Securities Act itself, that any condition, stipulation or provision to waive compliance with any provision of the act or rules or regulatons under it shall be void.

Congress has shown a consistent policy in these acts to state the circumstances in which contracts or parts of contracts shall be illegal and the consequences which shall flow from specified violations of the act. In particular, § 29 of the Securities Exchange Act of 1934, *supra*, shows that if Congress has in mind that a contract shall be void in any aspect it has in this group of statutes demonstrated its ability so to provide.

Cases under State Blue Sky Laws are not here persuasive. Those cases treating the effect of sales of unregistered or unlicensed securities in violation of a particular act are extensively dealt with in the note in 87 A.L.R. 98. (This note supersedes, 87 A.L.R. 42-43, the note in 67 A.L.R. 716, [and a number of earlier annotations] which was relied upon by the court below. R. 234.) The majority of the cases hold that a sale in violation of the particular act is outright void. In many instances this is the result of a direct statutory mandate to that effect. In other instances invalidity was thought by the court to rise from the penal provisions of the act, etc. Many of the laws,[17] however, have been amended to make sales in violation of the act voidable at the election of the purchaser. 87 A.L.R. 101. And in some jurisdictions the state courts have upheld contracts for sale of stock in violation of the act, considering that the legislature did not intend, in the particular statutes there under consideration, to make contracts void, but only to subject viola-

[17] The Uniform Sale of Securities Act, adopted by the National Conference of Commissioners on Uniform State Laws in 1929 (9 Uniform Laws Annotated 387) contains one form of statutory provision. Section 16, dealing with "remedies" provides that "Every sale made in violation of any of the provisions of this act shall be voidable at the election of the purchaser," and that certain persons in addition shall be liable upon a rescission, in a manner provided. It is significant that in one jurisdiction, Oregon, which adopted this statute, the equivalent of Section 16 provides that a sale made in violation of the act shall be *void*. *Id.*

tions of the law to the penalties expressly prescribed by the legislature. 87 A.L.R. 103.[18] It is the last-mentioned group of cases which, we believe, most nearly approach the present case.

III.

This is Not a Transaction "Involving Any Public Offering".

The court below held that the transaction involved amounted to a public offering, so that the stock of respondent was not exempt from registration under § 4(1), clause 2, of the Securities Act. The court took the position that the option agreement itself and the so-called subsequent modifications by letter recognized that petitioner was "selling the treasury stock to all and sundry," and that this practice, as well as the case of *Securities and Exchange Commission* v. *Sunbeam Gold Mining Co.* (C. C. A. 9th, 1938), 95 F. (2d) 699, made it apparent that the offering was public.

The decision below rests upon a misapprehension. The only offer in question or before the court is the standing offer of the option agreement itself to sell shares of stock to petitioner, provided petitioner made certain payments. That was an offer to sell all the stock of the corporation remaining in its treasury to but one person, petitioner. The offer was not to the public at large, nor, in fact, to the public at all. It was in no sense a public offering.

---

[18] In addition to the cases listed in the annotation, see *Fosdick* v. *Investors Syndicate*, 266 N. Y. 130, 135; *Cochran* v. *Hurth*, 29 Ohio App. 305, 163 N. E. 560, 561; *Sajor* v. *Ampolin*, 275 N. Y. 125, 131, 9 N. E. (2d) 803, 805-806; *H. H. Miller Industries Co.* v. *Roman*, 37 Ohio App. 71, 174 N. E. 141. *Cf. Robertson* v. *Business Boosters Country Club*, 212 Ala. 621, 622-623, 103 So. 576, 577; *Doherty* v. *McAuliffe* (C. C. A. 1st, 1935), 74 F. (2d) 800, 802-803, cert. den. 294 U. S. 730. This viewpoint seems to be the modern tendency.

If petitioner sold, in turn, some of the shares it received; or if respondent sold, as it was permitted to under the modification of the original agreement of May 11, 1935 (R. 212), certain of the shares to which petitioner was entitled, that is a matter quite apart from the issue raised by this action. The nature of the offerings in such instances—or, indeed, the identity of the purchasers, whether members of the public or not—was not in issue or shown by the testimony in this case. If those sales were pursuant to offerings subsequently made to the public so that the shares ought to have been registered before they were sold, that is a matter not affecting the necessity for registration so far as sales to petitioner are concerned.

We recognize that the question of whether an offering is of a public nature is very largely a question of fact. See Opinion of the General Counsel, Securities and Exchange Commission, Release No. 285, Compilation of Releases under the Securities Act of 1933, Gov. Print. Off., 1937, p. 87; Susman, *Exempted Transactions under the Securities Act of 1933*, 24 Wash. U. L. Q. 383, 386. Cf. Viscount Sumner in *Nash* v. *Lynde* [1929] A. C. 158, 169; Douglas and Bates, *Some Effects of the Securities Act upon Investment Banking* (1933), 1 U. Chic. L. Rev. 283, 299, note 61. We recognize also that a distinction is to be observed between the sale itself and the offering; there would be no escape from registration, though the sale were private, if the offering pursuant to which that sale were made were a public offering. Cf. *Black* v. *Solano Co.* (1931), 114 Cal. App. 170, 177-178, 299 P. 843. But here, it is obvious on the face of the offering that was made that it was to but one person; and that person (petitioner) took an active interest and possessed a special knowledge of the affairs of respondent—as witness the provision of the agreement (R. 177) and the modification of the agreement

of May 11, 1935 (R. 212-213) as to the use to which the proceeds received by respondent for the stock were to be put. *Securities & Exchg. Comm.* v. *Federal Compress & Whs. Co.* (W. D. Tenn., 1936), C. C. H. Securities Act Service ¶ 2203.09, app. dismissed without prejudice (C. C. A. 6th, 1937), 88 F. (2d) 1018. Cf. *Sherwell* v. *Incandescent Mantles Syndicate* (1907), 23 T. L. R. 482, 51 Sol. Jo. 446; *People* v. *Ruthven* (1936), 160 Misc. 112, 288 N. Y. Supp. 631, 636-637.

The reliance of the court below, therefore, on sales made to "others" (see Exhibit 74) seems misplaced. *Black* v. *Solano Co., supra.* So far as the offer in suit is concerned, the case comes within Rule 152 of the Securities and Exchange Commission (Release No. 305, Mar. 2, 1935, S. E. C.; C. C. H. Securities Act Service, ¶ 5152):

> "The phrase 'transactions by an issuer not involving any public offering' in Section 4(1) of the Securities Act of 1933 shall be deemed to apply to transactions not involving any public offering at the time of said transactions although subsequently thereto the issuer decides to make a public offering and/or files a registration statement."

Moreover, there is nothing in the record to support the statement of the court below that petitioner was "selling the treasury stock to all and sundry." There is no evidence that petitioner (or its president, Mr. Frost, who conducted all transactions for it) ever undertook the sale of any of the treasury stock in question, whether already received by petitioner or still in the treasury of respondent, except possibly with respect to the sale of 80,000 shares to E. J. Gibson & Co., and with respect to that sale, the shares were in respondent's treasury [19] and never were in petitioner's hands.

[19] Even as to these shares, at the trial, Mr. Nuzum, respondent's president, testified he had taken the position that petitioner "had nothing to do with getting the sale" of 80,000 shares of stock to Gibson (R. 142).

The reliance of the court below upon *Securities & Exchange Comm.* v. *Sunbeam Gold Mining Co.* (C. C. A. 9th, 1938), 95 F. (2d) 699, is likewise a misapprehension. That case concerned an offering to 530 individuals, including all the stockholders of two companies which were to be merged. In the present case, we have an offer to but one person, petitioner; and there is not the remotest reason to suspect that that offer was consequent upon any offering to the public or was merely a part of such a public offering.

On the contrary, the fact that petitioner undertook to purchase the entire 1,300,000 shares which remained in the treasury of respondent (R. 175) put it beyond the power of respondent to offer any shares to the public while the agreement remained unchanged. It is true that because petitioner later became involved in financial difficulties it subsequently waived its right to take certain of the treasury shares so that they might be sold; but there is nothing to show how this converted the transaction into a "public offering." The rule is that "It is not to be presumed the parties intended to make a contract which the law does not allow." *Bank of Kentucky* v. *Adams Exp. Co.*, 93 U. S. 174, 181. "A contract is not to be assumed to contemplate unlawful results unless a fair construction requires it upon the established facts." *Cincinnati, P., B. S. & P. P. Co.* v. *Bay*, 200 U. S. 179, 184; see *Hobbs* v. *McLean*, 117 U. S. 567, 575-6.

Also, Mr. Frost himself had noted, February, 1935, Ex. 67, that Mr. Nuzum had "talked with Mr. Lilly of Gibson & Company" respecting calls for more stock of respondent. The sale to Gibson & Company was in May, 1935 (Exs. 32, 74; R. 74). On the other hand, Mr. Frost testified, in showing that the monthly payments on the contract had been met in part from proceeds of treasury stock sold other persons, that "* * * prior to the date of the next payment I made that sale to Gibson" (R. 74). He later testified (R. 86) that he himself sold the 80,000 shares [to Gibson] and that the sale of 20,000 shares to J. E. Jones was with his consent.

Accordingly, the situation is one in which a private, not public, offering was made to petitioner; and the registration of the shares was unnecessary under the Securities Act. Even, therefore, if contracts are invalid by which the parties seek to deal in shares which ought to be registered under that act, but which are not, that rule would have no effect here; for the shares are exempted by Sec. 4(1) of the act.

Conclusion.

The judgment of the Supreme Court of Idaho should be reversed.

Respectfully submitted,

ERNEST L. WILKINSON,
CHARLES J. KAPPLER,
JOHN W. CRAGUN,
Counsel for Petitioner.

APPENDIX.

Statutes Involved.

Provisions of Securities Act of 1933, c. 38, 48 Stat. 74, as amended by the Securities Exchange Act of 1934, c. 404, 48 Stat. 881, 905, Title II.

Sec. 2. [15 U. S. C. § 77b] When used in this title, unless the context otherwise requires—

(1) The term "security" means any note, stock, treasury stock, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of interest in property, tangible or intangible, or, in general, any instrument commonly known as a security, or any certificate of interest or participation in, temporary or interim certificate for, receipt for, or warrant or right to subscribe to or purchase, any of the foregoing.

* * * * * * *

(3) The term "sale", "sell", "offer to sell", or "offer for sale" shall include every contract of sale or disposition of, attempt or offer to dispose of, or solicitation of an offer to buy, a security or interest in a security, for value; except that such terms shall not include preliminary negotiations or agreements between an issuer and any underwriter. * * *

* * * * * * *

(4) The term "issuer" means every person who issues or proposes to issue any security; * * *

* * * * * * *

(11) The term "underwriter" means any person who has purchased from an issuer with a view to, or sells for an issuer in connection with, the distribution of any security, or participates or has a direct or indirect participation in any such undertaking, or participates or has a participation

in the direct or indirect underwriting of any such undertaking; but such term shall not include a person whose interest is limited to a commission from an underwriter or dealer not in excess of the usual and customary distributors' or sellers' commission. As used in this paragraph the term "issuer" shall include, in addition to an issuer, any person directly or indirectly controlling or controlled by the issuer, or any person under direct or indirect common control with the issuer.

(12) The term "dealer" means any person who engages either for all or part of his time, directly or indirectly, as agent, broker, or principal, in the business of offering, buying, selling, or otherwise dealing or trading in securities issued by another person.

* * * * * * *

Sec. 4. [15 U. S. C. §77d] The provisions of section 5 shall not apply to any of the following transactions:

(1) Transactions by any person other than an issuer, underwriter, or dealer; transactions by an issuer not involving any public offering; * * *

* * * * * * * *

Sec. 5 [15 U. S. C. § 77e]. (a) Unless a registration statement is in effect as to a security, it shall be unlawful for any person, directly or indirectly—

(1) to make use of any means or instruments of transportation or communication in interstate commerce or of the mails to sell or offer to buy such security through the use or medium of any prospectus or otherwise; or

(2) to carry or cause to be carried through the mails or in interstate commerce, by any means or instruments of transportation, any such security for the purpose of sale or for delivery after sale.

(b) It shall be unlawful for any person, directly or indirectly—

(1) to make use of any means or instruments of transportation or communication in interstate com-

merce or of the mails to carry or transmit any prospectus relating to any security registered under this title, unless such prospectus meets the requirements of section 10; or

(2) to carry or to cause to be carried through the mails or in interstate commerce any such security for the purpose of sale or for delivery after sale, unless accompanied or preceded by a prospectus that meets the requirements of section 10.

* * * * * * *

Sec. 6. [15 U. S. C. § 77f] (a) Any security may be registered with the Commission under the terms and conditions hereinafter provided, by filing a registration statement in triplicate, at least one of which shall be signed by each issuer, its principal executive officer or officers, its principal financial officer, its comptroller or principal accounting officer, and the majority of its board of directors or persons performing similar functions (or, if there is no board of directors or persons performing similar functions, by the majority of the persons or board having the power of management of the issuer), and in case the issuer is a foreign or Territorial person by its duly authorized representative in the United States;

* * * * * * *

Sec. 12. [15 U. S. C. § 771] Any person who—

(1) sells a security in violation of section 5 or

(2) sells a security (whether or not exempted by the provisions of section 3, other than paragraph (2) of subsection (a) thereof), by the use of any means or instruments of transportation or communication in interstate commerce or of the mails, by means of a prospectus or oral communication, which includes an untrue statement of a material fact or omits to state a material fact necessary in order to make the statements, in the light of the circumstances under which they were made,

not misleading (the purchaser not knowing of such untruth or omission), and who shall not sustain the burden of proof that he did not know, and in the exercise of reasonable care could not have known, of such untruth or omission,

shall be liable to the person purchasing such security from him, who may sue either at law or in equity in any court of competent jurisdiction, to recover the consideration paid for such security with interest thereon, less the amount of any income received thereon, upon the tender of such security, or for damages if he no longer owns the security.

* * * * * * *

Sec. 14. [15 U. S. C. §77n] Any condition, stipulation, or provision binding any person acquiring any security to waive compliance with any provision of this title or of the rules and regulations of the Commission shall be void.

* * * * * * *

Sec. 17. [15 U. S. C. §77q] (a) It shall be unlawful for any person in the sale of any securities by the use of any means or instruments of transportation or communication in interstate commerce or by the use of the mails, directly or indirectly—

(1) to employ any device, scheme, or artifice to defraud, or

(2) to obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(3) to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser.

(b) It shall be unlawful for any person, by the use of any means or instruments of transportation or communication in interstate commerce or by the use of the mails, to publish, give publicity to, or circulate any notice, circular, adver-tise-

ment, newspaper, article, letter, investment service, or communication which, though not purporting to offer a security for sale describes such security for a consideration received or to be received, directly or indirectly, from an issuer, underwriter, or dealer, without fully disclosing the receipt, whether past or prospective, of such consideration and the amount thereof.

* * * * * * *

Sec. 20 [15 U. S. C. §77t] * * * (b) Whenever it shall appear to the Commission that any person is engaged or about to engage in any acts or practices which constitute or will constitute a violation of the provisions of this title, or of any rule or regulation prescribed under authority thereof, it may in its discretion, bring an action in any district court of the United States, United States court of any Territory, or the Supreme Court of the District of Columbia to enjoin such acts or practices, and upon a proper showing a permanent or temporary injunction or restraining order shall be granted without bond. * * *

* * * * * * *

Sec. 24. [15 U. S. C. §77x] Any person who willfully violates any of the provisions of this title, or the rules and regulations promulgated by the Commission under authority thereof, or any person who willfully, in a registration statement filed under this title, makes any untrue statement of a material fact or omits to state any material fact required to be stated therein or necessary to make the statements therein not misleading, shall upon conviction be fined not more than $5,000 or imprisoned not more than five years, or both.

Specification of Errors to be Urged.

1. The court erred in holding that the contract of September 10, 1934, as modified, violates the Securities Act of 1933.

2. The court erred in holding that the contract of September 10, 1934, as modified, is void.

3. The court erred in holding that the contract of sale and purchase of the shares of stock involved is not exempt from the provisions of Section 5 of the Securities Act of 1933 by reason of Section 4 of said Act.

4. The court erred in failing and refusing to enter judgment for petitioner.

5. The Court erred in entering judgment for respondent.

6. The court erred in finding and holding that petitioner sanctioned the sale of treasury stock to all and sundry.

Blank Page